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Prime Minister ^{cc/BO} ^{PC}

PRIME MINISTER

A very encouraging report, with an ambitious target for increasing our share of the Chinese market

UK TRADE MISSION TO CHINA AND HONG KONG
27th FEBRUARY - 13th MARCH 1985

CJD
15/3

1. I thought that I should report to you straightaway on my mission.

2. The participants on the mission were:

- Lord King, Babcock International
- Mr. R. Giordano, BOC
- Mr. J. Glasscock, British Aerospace
- Sir Eric Sharp, Cable & Wireless
- Mr. R. Kingdon, Davy McKee
- The Rt. Hon. James Prior, GEC
- Sir Duncan McDonald, NEI
- Mr. D. Jackson, Rolls Royce
- Mr. J. Swinglehurst, The Sedgwick Group
- Mr. H. Harrison, Simon Engineering.

My understanding is that they are unanimous in believing that their participation in the mission has been enormously worthwhile. They were particularly pleased by the level of our reception in China.

3. Our host was State Councillor, Madame Chen Muhua, Minister for Foreign Economic Relations & Trade.

- In Peking, we met Premier Zhao Ziyang
- Vice Premier Li Peng
 - Minister for Chemical Industry
 - Minister for Agriculture
 - Minister of Water Resources & Electric Power
 - Minister for Metallurgical Industry
 - Minister for Posts & Telecommunications
 - Deputy Chairman, State Planning Commission
 - Deputy Chairman, State Economic Commission
 - Managing Director, China International Economic Consultants Inc. (CITIC)

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In Shanghai, we met Mayor Wang Daohan
Vice Mayor Ruan Chong Wu
Director of Shanghai Municipal Foreign
Economic Relations and Trade Commission
President of Shanghai Investment & Trust
Corporation

In Canton, we met Governor Liang
Mayor Ye
Vice Governor Kun Ji

In Shenzhen, we met the Mayor and Vice Mayor.

4. In addition to these meetings, our hosts arranged numerous bilaterals between individual members of the mission and key officials in the enterprises related to their businesses. These provided the participants with an introduction to the key decision-makers which they told me they had found hard to obtain in the past. Overall, I am clear that the scale and warmth of our reception revealed a strong desire on the part of the Chinese to make the mission a success; indeed, individual Chinese remarked to us on a number of occasions that the scale of our reception was virtually without precedent.

RESULTS

5. In total eight agreements were signed by the members of the mission while in China. These are set out in detail in Annex 1.

6. Equally as important were the foundations laid for the future. Without exception, every company on the mission entered into discussions in areas in which they hoped to do substantial business. Negotiating contracts in these fields is everywhere a lengthy affair (let alone with the Chinese) but I am confident that the discussions held by the mission members will prove to have been an invaluable aid to the winning of some very major orders.

7. In your letter to Premier Zhao, which I delivered in the course of our meeting, you referred to three specific projects:

The BAe 146 Although the 146 contract was not signed during the mission (and at one time the prospects looked very bleak), Vice Premier Li Peng subsequently raised the matter with me and said that he was sure that a deal could be reached provided that both sides were prepared to compromise. A day later, Madame Chen said to me over dinner said that she hoped that a deal would be reached before Premier Zhao's visit to Britain. BAe are continuing their negotiations.

On the Daya Bay Power Station, Vice Premier Li Peng, to whom I delivered a letter from Peter Walker, said that he was now looking for a speedy conclusion of the negotiations and the award of a contract to GEC, subject to the final details being settled. I am given to understand that the delays lie with the French side but that GEC are confident of receiving a Letter of Intent by the Summer.

The Cable & Wireless agreement was signed.

8. I should perhaps mention that procedures in China differ to a degree from practices in the more industrialised world. There is little commercial law and agreements proceed by way of Letters of Understanding and Intent; and formal contracts come very late, if at all. Pilkington, for example, are already building their float glass factory in Shanghai without having signed the joint venture contract. Incidentally, I believe I was able to help them with some procurement problems associated with the venture.

9. More generally, it was made clear to us that the Chinese are looking to Britain as trading partners in a number of key sectors. These include power generation (where I was told that future requirements could amount to 300,000 megawatts); transmission lines (where we saw plans for many thousands of kilometres of DC and AC lines); telecommunications and steel mills (where we discussed projects which cumulatively will exceed the output of British Steel).

MESSAGES

10. The message repeated to us from Premier Zhao downwards was that the agreement on Hong Kong had opened up a new chapter in

Sino-British relations. Premier Zhao made special reference to the fact that the Japanese were unwilling to transfer technology - a theme that was repeated in many other meetings. I reiterated the assurances given by the members of my delegation that we would have no such inhibitions if the terms were right as we would wish to consider China a full partner.

11. Four particular items are worthy of note:

(a) Competitiveness This means simply that the Chinese expect the lowest possible prices in all agreements which they reach. To some extent, the continuing statements made to us about the need for competitiveness can be seen as a ritual incantation and one which is given similarly to all visitors from Western countries. Nevertheless, it is clear that, despite the fund of goodwill towards the UK, UK companies will benefit from this only if their proposals are seen by the Chinese to represent a good bargain in strictly commercial terms.

(b) Soft Loans Both Vice Premier Li and Madame Chen referred to our current policy of not providing soft money as potentially inhibiting the growth of our bilateral trade. The same message was given to a number of mission members in individual meetings with their Chinese counterparts. Our attitude was contrasted by the Chinese with that of other Western and EEC countries, a growing number of which are clearly prepared to provide mixed credit packages despite the agreement at the 1980 Venice Summit that such credits should not be offered to China.

I am clear that we should not over-react to such comments. In particular, where our technology is in advance of that on offer from our competitors, the Chinese will buy from us on normal credit terms. In addition, it needs to be remembered that the great bulk of China's foreign purchases are paid for in cash out of her substantial foreign exchange reserves and not on credit.

Nevertheless, I think that we may wish to look again at our present policy, to see whether there is some scope within existing resources for re-structuring our aid budget so that some form of it can be given in mixed loans to China for specific

areas. The kinds of area which I have in mind are those where we have yet to make a major breakthrough into the Chinese market but could do so if we were prepared to consider making soft money available in a strictly limited number of cases. This is something which it might be sensible to discuss further with colleagues concerned.

(c) Technology Transfer Much of our discussion with both Ministers and Heads of Enterprises was concerned with their desire to acquire technology and the realisation, in a changing technological world, that this would necessitate a joint venture. We were able to clarify many areas of doubt such as the term of a joint venture and the ability to remit both capital and profits and it became abundantly clear that the Chinese are now prepared to be much more flexible than in the past. Nevertheless, a problem remains where a potential joint venture is not able to generate sufficient foreign exchange to cover the profits being earned by the foreign partner.

(d) Invisibles Considerable interest in our financial and insurance sector was evidenced at all our meetings although it became clear that China's industry is structured in such a way that most matters of insurance are dealt with through the People's Insurance Company of China (PICC). Nevertheless, I believe there to be considerable scope for the financial sector (particularly in the provision of financial packages for future projects) and I would like to give some thought to ways in which we can build on the high regard in which the Chinese hold the City of London.

HONG KONG

12. The visit to Hong Kong provided a useful opportunity to stress that our drive for increased trade with China did not mean any lessening in our close relationship with Hong Kong. The simple fact is that Hong Kong is today three times more important to the UK as a market in its own right than China. I found little nervousness that we were lessening our commitment to Hong Kong but much criticism of the way that the vast bulk of investment in Hong Kong came from non-UK sources.

13. The attractions of Hong Kong as a gateway to China, particularly for the small and medium sized UK companies, cannot be over-emphasised. Indeed, Hong Kong based companies are already taking full advantage of this gateway in the wake of the Hong Kong Agreement.

FOLLOW UP

14. If we are to get the maximum out of this visit, we need to ensure that it is properly followed up. I shall be asking all those who were on the mission for a monthly report (copied to Paul Channon) on the progress they are making. We will all meet together in about six months. I would also hope that we can disseminate the lessons we have learned to other interested British companies.

15. The Chinese value both continuity and friendship. Indeed, Cable & Wireless have an edge, not only because of their technology but because Eric Sharp is universally regarded as an 'old friend' and he has invested much time and effort in the past three years to attain this status. This was a message not lost on our participants.

16. China is still a centrally planned economy despite some degree of devolution to the Provinces and the introduction of incentives to individuals. To a substantial degree, business decisions are political decisions. I think, therefore, it is important that we continue to have regular Ministerial contact with the Chinese on trade issues whenever possible by colleagues who are already familiar to them. I hope that it might always be possible to include businessmen on these visits since this mission has demonstrated that it can certainly facilitate the right level of contact.

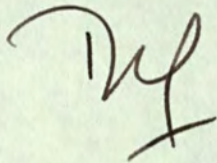
17. Overall, I am even more confident than when I departed of the enormous potential of China for us. No one who has either seen the pace of development which is currently taking place or heard their plans can fail to see the clear opportunity for foreign companies to participate in China's progress. There is still considerable ground to make up. Presently we account for about 1% of China's foreign trade compared with our overall share of world markets of between 5% and 6%. I see no reason why, with

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sufficient commitment, we should not raise our share of the China market to this level over the next few years.

18. I am copying this minute to Geoffrey Howe, Nigel Lawson, Peter Walker, Norman Tebbit and Paul Channon.

A handwritten signature in dark ink, appearing to be 'Dyf' or similar, written in a cursive style.

DY

15th March, 1985

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MEMORANDA SIGNED DURING THE MISSION

In total eight Memoranda were signed by members of the Mission in China and Hong Kong as follows:

BRITISH OXYGEN COMPANY

A Letter of Intent was signed which looks forward to the conclusion of a joint venture agreement involving the purchase by BOC of half of the Shanghai Chemical Company. The agreement will be subject to satisfactory terms being negotiated concerning the duration of the agreement and the repatriation of profits.

CABLE & WIRELESS

Three Memoranda were signed as follows:

1. A Memorandum of Intent to establish as a joint venture a telecommunications technology development centre in Peking with conference, office and hotel facilities.
2. A Memorandum of Intent to establish a joint venture to develop the telecommunications systems of the Yangtze Delta area. This will involve capital expenditure of \$500 million in the first five years.
3. A joint project agreement to provide modern telephone facilities in the Pearl Rive Delta including direct dialling with Hong Kong.

ROLLS ROYCE

A Protocol was signed in Peking recognising the imminent signature of a further contract worth some £16 million for the supply of Rolls Royce spey powered generating sets for the Nan Jiang oilfield.

SIMON ENGINEERING

Three Memoranda were signed as follows:

1. A Memorandum of Understanding with the Peking Food Bureau on food processing developments and food machinery manufacture. The venture will involve the initial importation of complete plants followed by the establishment of a joint venture company manufacturing food processing plant.
2. A Memorandum of Understanding on food processing development and food machinery manufacture with the Shanghai Food Bureau along similar lines to the Peking agreement.
3. A Memorandum of Understanding for co-operation in food processing industries in Jiangxi Province, including the supply of a complete flour mill.